



Research Article

The State of Economic Development in Nepal

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Abstract

This paper highlights the importance of measuring poverty through a multitude of approaches. This paper also discusses the current economic condition of Nepal using indices that emphasize financial aspects as well as by using indices that go beyond commercial elements. The overarching goal of this paper is to provide a comprehensive understanding of the state of poverty and economic development in Nepal. The findings of this paper suggest that proper access to cooking fuel, education facilities, and adequate nutrition are the binding constraints on Nepal's developmental aspirations. Targeted investment in these areas will certainly help to reduce widespread poverty.

Keywords: economic development; poverty; living standard; poverty indices

Introduction

To devise effective policies for poverty reduction, it is necessary, first, to measure poverty holistically. Without adequate information on poverty, it is difficult, if not impossible, to design efficient development strategies. The World Bank publication, *Introduction to Poverty Analysis* (2005), for example, mentions that there are mainly four reasons as to why there should be a comprehensive assessment of poverty (Khandker, 2005):

1. To keep the poor on the agenda
2. To target interventions, domestically and worldwide
3. To monitor and evaluate projects and policy intervention geared towards the poor, and

4. To assess the effectiveness of institutions whose goal is to help the poor (Khandker, 2005).

While measuring poverty, scholars need to pay careful attention to the following rules. First, one must choose the appropriate indicator of well-being. Second, one must select a threshold (poverty line) below which households and individuals will be considered poor. Finally, researchers need to report findings not just at an aggregate level, but also at a disaggregated level, i.e., not only for the entire population but also for subgroups (Coudouel *et al.*, 2002).

There are monetary and nonmonetary indicators of poverty, and the latter is the focus of this study as it is more comprehensive and provides more accurate information on deprivations and their causes. However, we cannot downplay the role of the monetary approaches as they are often considered to be the starting point for most poverty

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analyses (Khandker, 2005). Nonmonetary measures help in devising effective poverty alleviation strategies. To prove this assertion, I provide a brief discussion of both the measures. I will also discuss the advantages and disadvantages associated with both the metrics.

The Monetary Indicators of Poverty

Under the monetary approach, individuals are considered poor if they fall below a certain threshold. The monetary dimension has been the dominant measure of poverty mainly because of the ease of calculation. The three most popular monetary indices measure the incidence of poverty (headcount index), depth of poverty (poverty gap index) and the severity of poverty (squared poverty gap index) (Coudouel *et al.*, 2002). Table 1 provides information on all three measures of poverty for three different time periods and for rural and urban areas of Nepal. These data are obtained from Nepal Living Standard Survey (NLSS), which publishes reports on Nepal's economic condition. The national poverty rate is set at Rs. 19,261² per annum for each household. The data is available only for years up to 2009/10.

According to the *headcount index*, which measures the proportion of the population that is poor, as of 2009, 25.16 percent of the total population falls below the poverty line (Ministry of Finance, 2011). Even though this index is easy to interpret, it has many shortcomings. First, it discounts the intensity of poverty. In other words, it does not discriminate between households that earn Rs. 500 per year and the ones that earn Rs. 10,000 in the same period, for example. Secondly, this measure puts households at the front and center. Khandker (2005) suggests that "the poverty estimates should be calculated for individuals and not households. If 20% of households are poor, it may be that 25% of the population is poor (if poor households are large) or 15% are poor (if poor households are small)" therefore the author posits that the only relevant figures for policy analysis are those for individuals. Thus, if we solely rely on

this measure to design poverty alleviation programs, we might end up redistributing income from the somewhat poor to the poorest households, which might not change the overall poverty level.

There are better measures of poverty available to researchers such as the *poverty gap index*. This index informs the extent to which individuals, on average, are below the poverty line. In the case of Nepal, data suggests that the *poverty gap index* has been declining over time for both the rural and urban areas; however, the gap is much more prominent for the rural area. This measure can be used to calculate the resources required to lift the country out of poverty. It is asserted that this measure helps determine "the minimum cost of eliminating poverty using targeted transfers is simply the sum of the entire poverty gap in a population" (Khandker, 2005). Even though this measure provides more information compared to the *headcount index*, it too falls short in providing a detailed picture of poverty. For example, it fails to capture the severity of poverty amongst the poor people, thus ignoring inequality among the poor. To remedy the shortcomings of this approach, policymakers use the *squared poverty gap index*.

The *squared poverty gap index* acknowledges the inequality among the poor. This approach places greater weight on those households that are relatively farther away from the poverty line. In simple terms, it provides the weighted sum of poverty gaps. For instance, a poverty gap of 15 percent is given a weight of 15 percent while one of 75 percent is given a weight of 75 percent. The virtue of using this approach is that unlike, for example, the *poverty gap index* – which weighs all poor households equally – it differentiates among the poor, thus providing a clearer picture of poverty for policymakers. However, it lacks intuitive appeal and is not a popular measure in development agencies (Khandker, 2005). For Nepal, the *Squared Poverty Gap* for rural area is nearly twice greater than that for the urban areas.

Table 1: Poverty Measures (in %)

Areas	(Poverty Headcount Index)			(Poverty Gap Index)			(Squared Poverty Gap Index)		
	1995/96	2003/04	2009/10	1995/96	2003/04	2009/10	1995/96	2003/04	2009/10
Nepal	41.76	30.85	25.16	11.75	7.60	5.43	4.67	2.70	1.81
Urban	21.55	9.55	15.46	6.54	2.20	3.19	2.65	0.70	1.01
Rural	43.27	34.62	27.43	12.14	8.50	5.96	4.83	3.10	2.00

(Source: Ministry of Finance, 2011)

² Throughout this study \$1 = Rs. 87.02 (the exchange rate as of April 23, 2013.)

The Non-Monetary Measure of Poverty

Since 1990, the UN has prioritized alleviating all forms of poverty. In other words, the UN suggests that countries should not only aim to achieve higher income per capita but should also focus on provisions of other factors that are important for a quality lifestyle. The deprivation that arises from low-income and consumption is captured by the *Human Development Index* (HDI). The UNDP describes HDI as a “summary measure for assessing long-term progress in three basic dimensions of human development: a long and healthy life, access to knowledge and a decent standard of living” (UNDP, 2013). As of 2012, Nepal ranked 144 out of 187 countries in HDI. Even though there have been significant improvements in the last five years, Nepal is still one of the least developed countries in the world. The table below presents data on HDI for Nepal between 2010 and 2015.

Table 2: Nepal’s HDI 2010-2015

Year	HDI Value
2010	0.529
2011	0.538
2012	0.545
2013	0.551
2014	0.555
2015	0.558

(Source: Human Development Report 2016)

The HDI is a holistic measure to gauge human development. However, it is not a foolproof measure. For instance, the score is calculated using only three above-mentioned factors: life expectancy, human capital, and the quality of life. Hence, in 2010 Oxford Poverty and Human Development Initiative (OPHI) developed a different measure: *Multidimensional Poverty Index (MPI)*, which significantly improves upon the previous measures. The MPI has three dimensions and ten indicators of well-being that are weighted based on their contribution to human suffering (Alkire & Maria, 2011). This index gives a higher weight to factors such as education and health and assigns less weight to living standards indicators such as access electricity, drinking water, sanitation, flooring, cooking fuel, and asset ownership. Following this convention, an

individual is considered MPI poor if they are deprived in one third or more of the weighted indicators.³ This measure helps create more effective anti-poverty measures. Unlike the other indices, this index depicts that many Nepalese are living in deprivation in one third or more of the weighted average (Alkire and Maria, 2011). Alkire and Maria (2011) find that most poor people face deprivation in areas such as cooking fuel, flooring of their houses, and sanitary provisions.

Conclusion

In this study, I discuss the general economic condition of Nepal. This paper highlights the importance of measuring poverty through different measures. To this end, this paper discusses the prevalence of income poverty for Nepal, which is measured by the *headcount poverty index*, the *poverty gap index* and the *squared poverty gap index*. However, income does not mean development because many people in the country might not have access to other resources required to maintain a quality lifestyle despite making reasonable income. Therefore, this paper also discusses the nonmonetary measures of poverty, namely the HDI and the MPI. The MPI, which is the most holistic measure of poverty, identifies the areas that warrant attention from all concerned bodies to expedite developmental activities in Nepal. More specifically, the MPI suggests that a clear majority of the population lack access to cooking fuel, proper floor, sanitation, education facilities, and proper nutrition. Targeted investment in these areas will certainly help improve Nepal’s economic condition.

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³See the graphical representation here: <http://ophi.org.uk/multidimensional-poverty-index/>, accessed 12/20/2017